United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

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75-7056

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United States Court of Appeals

For the Second Circuit.

SECURITIES & EXCHANGE COMMISSION

Plaintiff-Appellee,

-against-

SAMUEL H. SLOAN, individually and d/b/a
SAMUEL H. SLOAN & COMPANY

Defendants-Appellants

APPELLANT 'S REPLY BRIEF

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UNITED STATES COURT OF APPEALS
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-against-

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SAMUEL H. SLOAN, individually and d/b/a
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APPELLANT'S REPLY BRIEF

PRELIMINARY STATEMENT

The brief for the Securities & Exchange Commission argues that the S.E.C. has the general right to examine Sloan's books and records. Yet nowhere in the brief for the S.E.C. does it state from which rule or statute is this general right derived. The brief for the S.E.C. argues that Sloan has violated Rule 15c2-11 and was properly enjoined on that account. Yet nowhere in the brief for the S.E.C. does it point to any evidence which establishes that this rule has, in fact, been violated. On this point, the court should be referred not to the arguments advanced by the S.E.C. but to the language of the rule itself and the absence of any evidence in the record showing that this rule has been violated.

In fact, this case should be an easy one for this court to decide. The record contains so many grounds for reversal of the court below that the only problem lies in how far this court need go in finding error. For example, this court can decide the entire appeal on the grounds that the summons and complaint have never been properly served. Without proper service, jurisdiction does not attach and the court lacks the authority to proceed further in this case. It can be readily

seen from the docket sheet (A2) that no affidavit of service upon Samuel H. Sloan has ever been filed in this case. Rule 4(c) F.R. Civ. P. requires that service of all process shall be made by the U.S. Marshal, by his deputy, or by some person specially approved by the court for that purpose. Neither the Marshal nor his deputy has made any effort the serve the summons and complaint personally on Sloan nor has the court appointed any person specially for that purpose. Furthermore, final judgment was entered in this case before the normal twenty days to file an answer had run and therefore there was no opportunity to raise the issue of a jurisdictional defect in the court below.

However, Sloan and the S.E.C. have been in a state of continuous litigation for nearly five years and in the interests of finally bringing this litigation to an end, this court should probably decide all of the issues involved in this case, as it can do under the Declaratory Judgment Act 28 U.S.C. §2201, particularly since every significant issue must be resolved in favor of Sloan.

ARGUMENT

POINT I

THE S.E.C. HAS FAILED TO ESTABLISH ITS AUTHORITY TO EXAMINE SLOAN'S BOOKS AND RECORDS.

The brief of the S.E.C. makes much of Sloan's supposed failure to produce his books and records. However, only two pages of this brief (p. 16-17) deal with the question of whether the S.E.C. has a legal right to see Sloan's books and records.[1] On those pages, the S.E.C.

1. It should not be overlooked that Judge Ward made no fact findings regarding Sloan's supposed failure to produce books and records.

cites no rule or statute which requires Sloan to produce his books and records.

The cases cited on these two pages are of no aid to the S.E.C. The first case, S.E.C. v Olsen 354 F. 2d 166 (2d Cir. 1965) pre-dates Supreme Court decisions in See v City of Seattle 387 U.S. 541 (1967); Marchetti v United States 390 U.S. 39 (1968) and Grosso v United States 390 U.S. 62 (1968). Prior to See the prevailing rule was to be found in Frank v Maryland 359 U.S. 360 (1959) where a warrentless search was authorized to determine whether conditions existed which the Baltimore Health Code proscribed. 359 U.S. at 366. It was during this period that S.E.C. v Olsen was decided. However, Frank was overruled by See and by its companion case Camara v Municipal Court 387 U.S. 523 (1967) and therefore Olsen no longer has validity. Furthermore, Olsen involved the Investment Advisors Act of 1940 which is not at issue here.

Indeed, reliance by the S.E.C. on S.E.C. v Olsen is so misplaced that the mere citation of that case borders on deceit. Olsen turned on the immunity provisions of the Investment Advisors Act of 1940 then found at 15 U.S.C. 80b-9(d). A similar immunity provision then existed in §21(d) of the Exchange Act, 15 U.S.C. 78u(d). However, both immunity provisions were repealed by an Act of Congress dated October 15, 1970. P.L. 91-452, Title II, §216,84 Stat. 929. Thus, Olsen is irrevelant in this case and in any case presently brought under the Exchange Act.

Olsen in turn was based upon Shapiro v United States 335 U.S. 1 (1948), a case relied upon by the appellant but not by the S.E.C. Actually, the appellant believes that Shapiro is erroneous for the reasons stated in the dissenting opinion of Mr. Justice Jackson, 335 U.S. at 71, where that justice said:

"It would, no doubt, simplify enforcement of all criminal laws if each citizen were required to keep a diary that would show where he was at all times, with whom he was, and what he was up to. The decision of today, applying this rule not merely to records specially required under the act but also to records 'customarily kept' invites and facilitates that eventuality."

This statement is almost identical to the argument advanced by the appellant in opposing the temporary restraining order. (A62). Nevertheless, in the Marchetti and Grosso decisions, Shapiro was explained and qualified by the Supreme Court to the point that the "required records" doctrine does not help the S.E.C. and in fact helps the appellant. Among other things, Shapiro involved an immunity provision similar to that which existed in Olsen. As noted previously, no immunity provision exists in the case at the bar so that if Sloan were to surrender his books and records to the S.E.C. the door would be left open to a criminal prosecution which the S.E.C. admits it cannot bring if the books and records are not made available. Furthermore, even if the S.E.C. were to bring nothing more than civil action to enjoin a violation of a criminal statute, this would interfere with Sloan's liberty just as certainally as would a criminal prosecution or a criminal contempt proceeding.

It should be clear from this lawsuit that Sloan is merely asking for the right to be left alone; a right which all other persons, save stockbrokers, seem to enjoy. Certainally, after having been compelled to spend four years of his life defending one lawsuit brought by the S.E.C., Sloan is entitled to take such steps as will bring an end to this otherwise interminable litigation. If this court were to affirm the order and judgment of the court below the result would be to give the S.E.C. the authority to sit in Sloan's office day after day and look over his shoulder or the shoulder of his bookkeeper in order to wait for a bookkeeping error to be made so that the S.E.C. could rush into court and ask that Sloan be held in criminal contempt. This is no exaggeration of the power the

S.E.C. sees itself as having as is demonstrated by the fact that the S.E.C. seeks the drastic remedy of injunctive relief when it has not even taken the trouble to serve a subpoena duces tecum and has generally expressed only a cursory interest and sometimes no interest in actually examining Sloan's books and records.

The S.E.C. contends that See v City of Seattle, supra was distinquished by S.E.C. v Brigadoon Scotch Dist. Co. 480 F. 2d 1047 (2d Cir. 1973). However, that latter decision is irrevelant. S.E.C. v Brigadoon Scotch Dist. Co. involved an attempt by the S.E.C. to enforce an administrative subpoena. However, no administrative subpoena has been issued in this case. It appears that the S.E.C. is contending that Sloan is free to produce his books and records in Central Park, at the offices of the S.E.C. or at some other location "easily accessible" to the S.E.C. and therefore no physical entry into private premises is required and hence no Fourth Amendment claim can be made. (Brief for S.E.C. p. 16 n.14). However, the Supreme Court specifically rejected a similar claim in See as follows:

> "[W]e find untenable the proposition that the subpoena, which has been termed a 'constructive search,' Oklahoma Press Pub. Co. v Walling 327 U.S. 186, 202 (1946) is subject to Fourth Amendment limitations which do not apply to actual searches and inspections of commercial premises." 387 U.S. at 545.

Furthermore, in the case at the bar, Sloan has been enjoined solely because he refused to grant access to his apartment and therefore See clearly applies. The letter referred to on p. 5 of the S.E.C.'s brief which the S.E.C. conveniently elected not to offer as evidence makes it clear that members of the S.E.C. staff would be coming to Sloan's apartment on December 26, 1974 and that Sloan would be free to go about his business so long as the records were produced "immediately." No subpoena duces tecum or administrative summons was ever issued. No witness fees were tendered to Sloan. Nowhere in the brief of the S.E.C. is any reason

given as to why the S.E.C. should be permitted to examine Sloan's books and records other than the general desire by the S.E.C. to see if Sloan is in compliance with the S.E.C.'s bookkeeping rules and the prior injunction. Again, S.E.C. v Brigadoon Scotch Dist. Co. does not apply because there the S.E.C. sought access to the books and records for the specific purpose of determining if the "warehouse receipts" sold by Brigaddon were investment securities as defined by the Exchange Act. No such specific purpose is cited in this case. Instead, the S.E.C. is seeking to establish that it has the general right to peruse Sloan's records whenever it feels the desire to do so.

The remaining case relied upon by the S.E.C. is S.E.C. v Radio Hill Mines Co., Ltd. 479 F. 2d 4 (2d Cir. 1973) cert. denied 410 U.S. 941 (1973) which was grounded upon California v Byers 402 U.S. 424 (1971). The latter was a Supreme Court decision singularly unhelpful to the S.E.C. Byers was a 4-1-4 decision which upheld the validity of a California "hit and run" statute against a Fifth Amendment attack. There, the plurality opinion noted that the statute only required Byers to give his name and address. Nevertheless, even in that circumstance, four Supreme Court justices were strongly of the opinion that the giving of a name and address might form a "link in a chain of testimony needed to prosecute" Byers for a crime. 402 U.S. at 459. The limited intrusion upon Byers' claimed rights involved in the giving of his name and address was slightly extended by this courts decision in S.E.C. v Radio Hill Mines Co., Ltd. There the appellant, one Sidney Stein, was required to provide a list of all securities which he owned. Since the ownership of securities could not of itself be illegal, this court rejected Stein's Fifth Amendment claims.

The case at the bar, however, is entirely different. The S.E.C. wants to see Sloan's books and records in order to determine if Sloan is

violating the S.E.C.'s bookkeeping and record keeping rules, primarily Rules 17a-3 and 17a-4. If, for example, it turns out that the books do not exist, this in itself would form the basis for a criminal prosecution by the S.E.C. The pivotal judge in Byers decided in favor of the California "hit and run" statute on the ground that in most cases individuals involved in traffic accidents are not subjected to criminal prosecution and therefore the fears of most individuals who are forced to comply with this statute are an "imaginary possibility" as opposed to a "real and appreciable danger." However, no one including the S.E.C. would seriously argue that Sloan's fears of prosecution in this case reflect anything but a "real and appreciable danger." The S.E.C. has clearly stated that if it finds some deficiency in Sloan's bookkeeping it will prosecute. Therefore, this is precisely the kind of situation where Sloan has a complete Fifth Amendment defense.[2]

It should be noted that the S.E.C. bookkeeping rules require much more than a mere listing of securities owned as required in S.E.C. v Radio Hill Mines Co., Ltd. Rule 17a-3 requires all brokers to make and

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2. The brief for the S.E.C. states (p. 17) that the appellant has not directly addressed the Fifth Amendment question. However, several cases cited in the appellant's main brief deal with Fifth Amendment claims. See Marchetti v United States supra and Grosso v United States, supra. A detailed analysis of the Fifth Amendment arguments based on those decisions was unnecessary since the decisions speak for themselves. Other cases cited in the appellant's main brief, such as Boyd v United States 116 U.S. 616 (1886) involve Fourth and Fifth Amendment claims made concurrently. It often happens in cases where the production of books and records is sought that both Fourth and Fifth Amendment claims can be made. Another relevant case, not previously cited, is Spevak v Klein 385 U.S. 511 (1967) which held that because of the Fifth Amendment a lawyer could not be required to produce his books and records in a disbarment proceeding. In the case at the bar Selvers responded to Fifth Amendment arguments in the court below (A93) and it certainally cannot be said that this argument has not been preserved.

keep current blotters (or other records of original entry) containing an itemized daily record of all purchases and sales of securities, all receipts and deliveries of securities (including certificate numbers), all receipts and disbursements of cash and all other debits and credits; ledgers reflecting all assets and liabilities, income, expense and capital accounts; ledger accounts itemizing separately as to each cash and margin account of every customer and of such member broker dealer and partners thereof; all purchases, sales, receipts and deliveries of securities and commodities and all other debits and credits; ledgers reflecting securities in transfer, dividends and interest received, securities borrowed and loaned, moneys borrowed and loaned together with a record of the collateral therefore; all securities failed to receive and failed to deliver, all long and short stock record differences, a securities record or ledger reflecting for each security all "long" and "short" positions showing the location of all securities long and the offsetting position of all securities short; a memorandum of each brokerage order, and of any other instruction given or received for the purchase or sale of securities, whether executed or unexecuted; a memorandum of each purchase and sale showing the price and the time of the execution; copies of confirmations of all purchases and sales of securities and copies of notice of all purchases and sales of securities and copies of notice of all other debits and credits for securities, cash and other items; a record of all puts, calls, straps, stips, spreads, straddles and other options; a record of the proof of money balances and of all ledger accounts in the form of trial balances; a record of the computation of aggregate indebitedness and net capital as of the trail balance date; and all questionaires and applications for employment. The rule also provides for numerous exceptions. In view of the "required records" standards set by Shapiro v

United States, supra; Marchetti v United States, supra and Grosso v United States, supra it is inconceivable that the Federal Government can constitutionally require one of its citizens to "make and keep current" records of this volume and nature.

If the S.E.C. had never seen Sloan's books and records it might have a more reasonable case. However, the S.E.C. has examined Sloan's books and records on numerous occasions. Although an S.E.C. investigator first examined Sloan's records in 1970, the earliest date of an S.E.C. examination now involved in litigation occurred on January 12, 1971. At an administrative hearing and at the subsequent trial before Judge Ward, Arthur Bruder ("Bruder") an S.E.C. staff investigator testified that he visited Sloan's office and examined his records on January 12, 13, 14, and 25, 1971. At the administrative hearing Bruder testified that on one of these occasions he spent approximately six hours examining Sloan's records. (Tr. of record p. 67). Bruder made other visits in January and February, 1971 and then retired from the S.E.C. He was replaced by Sheldon Kanoff who visited Sloan's office on various dates in March, April, May, June, and August, 1971. On May 29 and 30th, 1973 George Appoldt and Frank Fraumeni, also investigators for the S.E.C., spent two full days in Sloan's office examining his records. There were many other visits not reflected in litigation because, in those cases that the S.E.C. claims to have found no violation, it seems unwilling to admit that any visit actually took place. However, at the first trial before Judge Ward, Nortman, staff attorney for the S.E.C. stated: (Tr. 638, line 16):

> "We will stipulate that the records are available for our perusal."

It is only reasonable that after four years of continuous harassment and litigation over the records that Sloan would at some point draw the line and state that S.E.C. investigators are no longer welcome in Sloan's office or apartment. However, the fact remains that from May of 1970 when Sloan first became a broker dealer, until November 6, 1974, S.E.C. investigators were given free access to all of Sloan's records.

Sloan has not waived any constitutional right by previously granting access to his records, see Garrity v New Jersey 385 U.S. 493 (1967), particularly since his refusal to show the S.E.C. investigators his books and records on this one occasion resulted in the revocation of his broker dealer registration. As noted previously, the S.E.C. has never issued a subpoena duces tecum nor does it cite any statutory authority for the proposition that it must be permitted to examine Sloan's books and records. In the court below, the S.E.C. claimed that such a right existed under §17(a) and Rule 17a-4. However, the amended version of §17(a) is of no aid to the S.E.C. As for Rule 17a-4, this rule is entitled "Records to be Preserved by Certain Exchange Members, Brokers and Dealers." The rule deals solely with the preservation of records. The S.E.C. has relied on subsection (a) and similar subsections. However, subsection (a) in pertinent part states:

> "Every member, broker or dealer.... shall preserve for a period of not less than six years, the first two in an easily accessible place, all records required to be made....."

The S.E.C. has contended that this language contains an implied right of inspection. However, it should be obvious that no implied right of inspection exists in Rule 17a-4. Furthermore, even assuming arguendo that such an implied right of inspection exists, that rights, particularly since it is not explicitely stated, is void for vagueness. Connally v

General Construction Co. 269 U.S. 385, 391 (1925); United States v Harris 347 U.S. 612, 617 (1954); Papacristou v City of Jacksonville 405 U.S. 156, 165-171 (1972); Grayned v City of Rockford 408 U.S. 104, 108-9 (1972); Smith v Goguen 415 U.S. 566, 575 (1974).

The point was made in the appellants main brief, and it bears repeating, that Fourth and Fifth Amendment defenses are not available to corporations. California Bankers Association v Schultz 416 U.S. 21, 55 (1974). Therefore, even if S.E.C. v Brigadoon Scotch Dist. Co. were not otherwise inappropriate, that decision would have no bearing on the case at the bar for the simple reason that Brigadoon Scotch Dist Co. is a corporation. It is submitted that there is overwhelming case law which establishes that the S.E.C. registration and reporting requirements, as applied to individuals, are unconstitutional. A case on point is Albertson v Subversive Activities Control Board 382 U.S. 70 (1965). That case declared unconstitutional the requirement that all members of the Communist Party register as such with the federal government. The opinion of the court was that the registration requirement was invalid on Fifth Amendment grounds since Congress deemed Communist Party members to be a "selective group inherently suspect of criminal activities." 382 U.S. at 79. It is probably fair to say that if a reasonable sample of average men on the street were asked whether they considered Communist Party members to be "inherently suspect of criminal activities" few would say yes; whereas if the same sample were asked whether stock brokers were considered to be "inherently suspect of criminal activities" the response would be overwhelmingly against the stock brokers. This, of course, is due to an intensive anti-stock broker campaign on the part of the S.E.C. The flames of anti-stock broker sentiment have been fanned, no doubt, by widespread losses in the securities markets but it has been the S.E.C. that has continuously harped on the theme that losses in the securities markets are

the result of fraud on the part of stock brokers. Virtually every major stock brokerage firm has been accused by the S.E.C. at one time or another of some sort of violation of S.E.C. rules and, since a violation of S.E.C. rules is criminal (see §32 of the Exchange Act 15 U.S.C. 78ff), it is fair to say that all stock brokers are "inherently suspect of criminal activities." Therefore, the S.E.C. broker dealer registration requirements are unconstitutional.

On the authority of Albertson as well as Marchetti and Grosso which followed, most laws which require various special classes of individuals to register with the federal government have been declared unconstitutional. In Haynes v United States 390 U.S. 85 (1968) the Supreme Court declared unconstitutional the requirement that owners of sawed-off shotguns register with the Secretary of the Treasury. In Timothy Leary v United States 395 U.S. 6 (1969) the Supreme Court declared unconstitutional the requirement that individuals who bring marijuana into the country must register that marijuana and pay a federal marijuana transfer tax. Since that time Congress on its own initiative has repealed law which required, among other things, that nariotics smugglers register as such with the Federal Government. See former 26 U.S.C. §§4701-4776. These cases, incidently, are supplied courtesy of the brief of the S.E.C. since California v Byers, which the S.E.C. believes to be favorable to the S.E.C., was careful to distinguish that ruling from Supreme Court rulings in Albertson, Marchetti Grosso and Haynes. 402 U.S. at 429.

In summary of this point, the S.E.C. has cited no statutory authority which gives the S.E.C. the right to examine Sloan's books and records and has not issued a subpoena duces tecum and, in any event, even if the reverse were true, Sloan would still have a complete Fourth and Fifth Amendment defense in the circumstances here. It must be added that it is ironic

the S.E.C. at one point has seemed to argue that the requirement that certain records be made and preserved by a broker implies that the S.E.C. has the right to see these records on the theory that otherwise the requirement would have no purpose. Since this argument implies that the brokers would not otherwise keep the records were they not required to do so, the conclusion is quickly reached that under the "required records" doctrine it is unconstitutional to require that these records be made because they would not be "customarily kept."

POINT II

THE BRIEF OF THE S.E.C. FAILS TO DEMONSTRATE THE VALIDITY OF RULE 15c2-11.

It is only to be expected that the brief of the S.E.C. would present arguments in a light most favorable to the S.E.C. However, even without opposition the arguments advanced by the S.E.C. are so unmeritorious that they would fall of their own dead weight. Rule 15c2-11 is clearly invalid and the arguments already presented in the appellants main brief need not be repeated here. In fact, Rule 15c2-11 is so invalid that there are many different legal theories which lead to the same result. The S.E.C. argues that Rule 15c2-11 has received the implicit approval of Congress. (Brief for S.E.C. p. 15). However, this is not the case. Congress specifically directed the S.E.C. to amend the present Rule 15c2-11 and the S.E.C. has as yet failed to do so. This circumstance demonstrates the point that Congress lacks the power to abrogate a rule of the S.E.C. only the courts can perform this function. The Senate report which the S.E.C. claims to support Rule 15c2-11 was in fact critical of S.E.C. rule making action in a number of specific instances and, for this reason, set up a hearing procedure which the S.E.C. must go through before it promulgates any more rules. Also Congress made immediate judicial review of S.E.C. rules available for the first time. §25(b) of the Exchange Act (15 U.S.C. 78y (b)).

The Senate report in question makes it clear that it expects the Court of Appeals to subject all S.E.C. rules to "searching" judicial scrutiny. It is clear that in this case under any searching scrutiny, Rule 15c2-11 must be declared invalid.

In addition, Rule 15c2-11 must be held constitutionally invalid under Lochner v New York 198 U.S. 45 (1905). Lochner held that the proper test of the validity of a criminal statute was whether the exercise of legislative power is rationally related to a legitimate legislative goal. In other words, the question is whether the means is appropriate to reach the goal.[3] In Lochner an employer received a prison sentence for permitting a baker to work more than 60 hours a week. The Supreme Court declared the law under which the employer was convicted to be unconstitutional. That judgment stands to this day.

The intent of rule 15c2-11 is to make it a violation of a criminal statute for a broker to quote the price of a security at a time when the issuer of that security has failed to file a financial report with the S.E.C.[4] In practical consequence, one effect of the rule is to make it difficult if not impossible for anyone to buy or sell any security which has ever been suspended from trading by the S.E.C. because such a suspension has a ten day duration and therefore keeps the security from being quoted in the pink sheets for more than four business days in succession, the

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4. To quote Gilbert and Sullivan, the question can be put another way by asking whether "the punishment fits the crime."

5. The principal exception found in the rule occurs in the case of a sucurity which has been quoted on a continuous basis. However, at oral argument in Sloan v S.E.C. 74-2457 counsel for the S.E.C. characterized a related exception as a "loophole" in the law indicating that the S.E.C. would like Congress to force all publically traded corporations to file with the S.E.C.

exception provided for by sub-section (f)(3) of the Rule 15c2-11 does not apply and it becomes illegal to quote the security. This point becomes clear because whenever the S.E.C. suspends trading in a security the S.E.C. issues a release which gives a brief statement of reasons for the suspension and concludes:

> "The Commission cautions broker-dealers, shareholders and prospective purchasers that they should consider carefully the foregoing information along with all other currently available information and any information subsequently issued by the company.
>
> Furthermore, brokers and dealers should be alert to the fact that pursuant to Rule 15c2-11 under the Exchange Act, no quotation may be entered unless and until they have strictly complied with all of the provisions of said rule. If any broker or dealer has any questions as to whether or not he has complied with said rule, he should not enter any quotation but immediately contact the staff of the Securities and Exchange Commission, Division of Enforcement in Washington, D.C. If any broker or dealer is uncertain as to what is required by Rule 15c2-11, he should refrain from entering quotations relating to the securities in question until such time as he has familarized himself with said rule and is certain that all of its provisions have been met. If any broker or dealer enters any quotation which is in violation of said rule, the Commission will consider the need for prompt enforcement action." [5]

If indeed it is fraudulent per se not to file a required report with the S.E.C., a remedy is available to the S.E.C. under §32 of the Exchange Act which authorizes criminal proceedings and sets a fine of not more than $100 per day for each day a report is filed late. For example, in the case at the bar, the S.E.C. contends that information concerning Franklin New York Corp. is not "publically available" which means in S.E.C. (brief p. 7) parlance that Franklin New York Corp. has not timely filed financial reports with the S.E.C. This, must be said, is not suprising since Franklin New York Corp. is in liquidation

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5. This fact was alleged in ¶65 of the complaint filed by Sloan in Sloan v S.E.C. et al 74 Civil 2792, U.S.C.A. docket no. 75-7283 and was admitted in ¶2 of the answer filed by the S.E.C.

under the Federal Deposit Insurance Act, 12 U.S.C. §1821. If indeed the officers of Franklin New York Corp. are violating the law by failing to file reports with the S.E.C. the remedy is to prosecute those officers and not to punish the innocent stock broker and thereby prejudice the rights of all public stockholders of Franklin New York Corp. who have committed no wrong and who wish lawfully to sell their security holdings. As far as the appellant is aware, neither the S.E.C. nor the U.S. Attorney have ever instituted a criminal prosecution based upon §32 of the Exchange Act which sought the assessment of the $100 per day fine which is provided for in that section. Thus the effect of Rule 15c2-11 is that innocent stock holders and stock brokers must suffer while corporate officers who have supposedly broken the law are allowed to go free.

It must also be mentioned that Lochner v New York is a decision which has been much maligned but which has never been overruled and its relevance here should be apparent. Everyone would agree that a state has a right to pass laws to promote the public health and welfare and to prevent fraud. However, under the Lochner test criminal penalties may not be imposed unless less drastic measures are unavailable. In the case of Rule 15c2-11, it should be obvious that there are ways to prevent fraud which fall short of the drastic measure of an absolute prohibition on the quotation of securities under threat of criminal penalties. Hence, Rule 15c2-11 is constitutionally invalid.

POINT III

THE REMAINING ARGUMENTS ADVANCED BY THE S.E.C. ARE WITHOUT MERIT.

The brief of the S.E.C. cites a plethora of cases which are either irrelevant to the action at the bar or which reach conclusions precisely the opposite from that which the S.E.C. claims they reach. For example,

in support of its argument that a temporary restraining order can never be appealed, the S.E.C. cites three cases (brief p. 18). However, in two of these cases this court decided that the temporary restraining orders in question were appealable. The third, Morning Telegraph v Powers 450 F. 2d 97 (2d Cir. 1971) was a case in which this court reversed the decisions of two district court judges which had denied motions to vacate temporary restraining orders. Aside from the many distinguishing features which are apparent from reading that decision, that case no longer constitutes a statement of the law because a recent Supreme Court decision, Granny Goose Foods v Teamsters 415 U.S. 423, 439-440 (1974), establishes that in removal cases of the type involved there a new rule applies whereby temporary restraining orders expire automatically. Thus, Morning Telegraph v Powers has no precedential value.

It must also be said that the S.E.C.'s claim that a temporary restraining order can never be appealed is particularly annoying. On September 29, 1975 Robert W. Herko and Beranrd L. Herman were found guilty by Judge Ward of criminal contempt for viclating a termporary restraining order entered by Judge Ward on January 24, 1975. S.E.C. v Saxon Securities Corp. et al 75 Civil 377. Exchange Act Rel. No. LR-7109, Oct. 8, 19 5. That temporary restraining order appears to have been similar to the one entered in the instant case in that the order directed the defendants not to violate the S.E.C.'s bookkeeping and net capital rules. Herko was sentenced to three months in prison.

This may be the first case in which a finding of criminal contempt has been made on an application by the S.E.C. without the involvement of the U.S. Attorney. This also may be the first case where anyone went to jail for violating the "highly technical" S.E.C. bookkeeping rule

(see S.E.C. v Reiter 146 F. Supp. 552 (S.D.N.Y. 1956)). It is submitted that there can be no doubt that if a person can be held in criminal contempt for violating even a temporary restraining order, that order is appealable. In fact, in one of the cases cited by the S.E.C. this court agreed, with this principle, observing that since a temporary restraining order must be obeyed it is necessarily appealable. This point is relevant to the case at the bar because this court should review the temporary restraining order particularly in view of Judge Wards predilection for holding individuals in contempt of court for violating temporary restraining orders which have long since expired.

The S.E.C. also cites cases such as S.E.C. v Shapiro 494 F. 2d 1301 (2d Cir. 1974) and S.E.C. v Culpepper 270 F. 2d 241 (2d Cir. 1959). These cases bear no resemblance to the action at the bar other than the fact that they provide instances in which the S.E.C. has been granted an injunction. The recent authoritative case which deals with the point the S.E.C. would like to make on p. 21 of its brief in S.E.C. v Management Dynamics ___ F. 2d ___ (2d Cir. 1975). However neither the S.E.C. nor Sloan is relying on that comprehensive decision here.[6]

The S.E.C. makes other claims but cites cases which do not support them. For example, on p. 24 of its brief, the S.E.C. argues that even if Judge Ward's findings of fact were found not to meet the requirements of Rule 52(a) F.R. Civ. P., the effect would be "non-jurisdictional" and a reversal would not be required. In support of this preposterous propo-

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6. Since no rule violation has been shown it goes without saying that no propensity to violate the rules has been demonstrated. However, in view of certain other arguments advanced by Sloan it would be inappropriate for him to cite S.E.C. v Management Dynamics. Furthermore, §21(e) of the Exchange Act has since been amended in a significant way so it is not clear if that decision constitutes a correct statement of the present law.

sition, the S.E.C. cites Sampson v Murray 415 U.S. 61, 87 (1974). However, an examination of page 87 of volume 415 of the U.S. Reporter does not reveal any support for the claim that a district court judge need not comply with Rule 52(a). Indeed, although the specific page in question deals with Rule 65 rather than Rule 52(a), the entire decision of Sampson v Murray reaches precisely the opposite result from which the S.E.C. urges here. The S.E.C. then goes on to cite a case in which this court affirmed a district court decision which denied a motion for a preliminary injunction even though no findings of fact were made. It is submitted that it should be obvious that the failure or refusal of the moving party to go forward with proof in support of its motion for a preliminary injunction should not act to prevent the district court from denying that motion. The burden of proof is clearly upon the moving party, Granny Goose Foods v Teamsters, supra 415 U.S. at 443, and if no proof is provided it would be difficult if not impossible for a district court judge to make any findings of fact at all. Nevertheless, in order to make possible adequate appellate review, Rule 52(a) makes it clear that findings of fact should be provided to the extent possible even in cases where the motion for injunctive relief is denied.

The S.E.C. next goes on to argue that even though Judge Ward did not make adequate fact findings, which is obviously the case here since, for example, the district court made no finding that Sloan violated Rule 17a-4 or that Sloan failed to grant the S.E.C. access to his books and records (see A172-173), this court should affirm Judge Ward's decision anyway because the "undisputed evidence in the record" demonstrates "Mr. Sloan's intentional disregard of the federal securities laws." (brief p. 25). However, this court is not permitted to do what the S.E.C. wants it to do. The S.E.C. in effect argues that since the dis-

trict court judge failed to do his job properly, the Court of Appeals should do it for him. However, with respect to inadequate findings of fact made by trial court, it is not the function of an appellate court to assume the powers of a trial court. Schilling v Schwitzer-Cummins Co. 142 F. 2d 82 (D.C. Cir. 1944). It has also been held that it is not the function of the Supreme Court of the United States to search the record and analyze the evidence in order to supply findings, which the trial court failed to make. Kelley v Everglades Drainage Dist. 319 U.S. 415 (1943) rehearing denied 320 U.S. 214, motion denied 321 U.S. 754. Appellate courts, under Rule 52(a), do not have the power to review evidence in the record and to supply findings of fact necessary to determine issues. Woods Constr. Co. v Pool Constr. Co. 314 F. 2d 405 (10th Cir. 1963). Furthermore, Judge Ward's self serving statement that "Mr. Sloan's only defense is that the foregoing statutes and regulations are unconstitutional," (A174) does not absolve the district court of the duty to make findings of fact particularly since it is clear from the record that Judge Ward's statement was, to put it bluntly, untrue. Among other things, Sloan has stated from the beginning his position that his acts or supposed failures to act do not constitute a violation of any statute or rule. In order for Judge Ward to comply with Rule 52(a) he would have been required to state what Sloan did or didn't do, what statute or rule this violated, and in what manner Sloan's acts or failures to act violated this statute or rule. Judge Ward's failure to do this constitutes a significant henderance to appellate review and for this reason alone he must be reversed.

The brief for the S.E.C. tries to make something of Sloan's failure to call Dolan as his witness (brief p. 10). On this point it should be said that an error occurs in the record on lines 23-24 of A146. The record should read as follows:

"MR. SLOAN: The next witness I wish to call is Mr. Dolan.

THE COURT: I think this would be a good point to take a five minute recess.

(Five Minute Recess)

MR. SLOAN: Your Honor, in view of an off the record discussion I have changed my mind and decided not to call Mr. Dolan---

During this five minute recess Judge Ward stood up and announced that Sloan would be wise not to call Mr. Dolan to testify because such testimony would only "hang" Sloan. Why Judge Ward made this gratuitous comment is not clear but in any event it is obvious that no inference can be drawn from Sloan's failure to call Dolan particular in view of Dolan's position as an investigator for the S.E.C.[7]

Another claim of the S.E.C. is that Judge Ward gave Sloan a fair hearing and, indeed, that Judge Ward gave Sloan "extraordinary latitude ...to present his case." (brief p. 20). Not only is there no basis for this claim but the S.E.C. demonstrates bad faith even by attempting to defend the conduct of Judge Ward. The actions of Judge Ward remind one of the trail of Sir Walter Raleigh in 1603. That trial has gone down as one of the most outrageously unfair trials in the history of English common law. In that case, Raleigh appeared pro se. After the jury had been selected and approved by Raleigh, the attorney general began the proceedings with a vicious attack on the character of the defendant, unfolding the details of his high offense as based on the written confession of one Lord Cobham. After he had concluded his opening address, the

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7. There appears to be no procedure for settlement of the transcript in the federal courts. This seems strange in view of Chessman v Teets 354 U.S. 156 (1957).

attorney general then introduced the written confession of Cobham, upon which the case against Raleigh chiefly defended. To this Sir Walter made reply:

> "If I knew any of these things, I would absolutely confess the indictment and acknowledge myself worthy a thousand deaths. Why, then, my Lords, let my accuser be brought and let me ask him a question and I have done; for if it may appear from his own relation that his accusation cannot be true, or he may be discovered by examination. If you condemn me upon bare inferences and will not bring my accuser to face, you try me by no law, but by a Spanish inquisition. If my accuser were dead or out of the realm, it were something; but my accuser lives and is in the house, and yet you will not bring him to my face."

Chief Justice Popham answered Raleigh's objection by reminding him that under a recent enactment affecting the rules of evidence, it was sufficient if proof were made either under hand or by testimony of witnesses or by depositions. Then followed the reading of testimony of others who confirmed the allegations made in Cobham's confession and the prosecution closed its case. Subsequently, the jury retired and in less than fifteen minutes returned a verdict of guilty. The Chief Justice then delivered the customary judgment in cases of this sort that the prisoner be drawn upon a hurdle to the place of execution, there to be hanged and cut down alive, disembowelled and quartered. The sentence was carried out fifteen years later.

In the case at the bar no explanation has been given by the S.E.C. as to why the two individuals who signed the affidavits which formed the basis for the S.E.C.'s motion were permitted to sit in the back of the courtroom without being called by the S.E.C. Judge Ward's decision to permit Sloan to "cross-examine" Spindler when Spindler gave no direct testimony and then to permit Sloan to testify in his own behalf was a hollow act since it is obvious that Judge Ward had already made up his mind about this case and nothing that the testimony was going to bring out would change his mind. Judge Ward also refused to permit Sloan to

call Selvers although the testimony of Selvers would obviously have been relevant.

In Jones v S.E.C. 298 U.S. 1, 28 (1936) the Supreme Court observed that the practices which existed in the time of the Stuarts which was when the trial of Sir Walter Raleigh took place, were among the intolerable abuses of the Star Chamber which brought that institution at the hands of Parliment in 1640. The Supreme Court further observed that the S.E.C. was attempting to revitalize these long discredited practices. Clearly, it has done so and an excellent example of the abuse of due process involved is the so-called hearing before Judge Ward. Judge Ward, like Chief Justice Popham, tried this case under no law. Judge Ward's conduct in this case and the case on appeal under docket no. 74-1436 is a disgrace to the federal judiciary. There can be no doubt that he must be reversed.

It is submitted that the law and the facts of this case are such that the judgment of the court below must be vacated and no further proceedings are necessary. However, in the event that there are further proceedings in the district court, it should be noted that the S.E.C. has not responded to the point that the decision of the Supreme Court in Curtis v Loether 415 U.S. 189 (1974) establishes that the defendant is entitled to a jury trial in cases of this sort. A subsequent decision Pernell v Southall Realty 416 U.S. 363 (1974) yields the same result. Thus, even if this court should fail to remove Judge Ward from this case, the prejudicial effect of the bias he has consistantly displayed should at least be somewhat diluted if this court directs that this case be

tried by jury.[8]

CONCLUSION

For all of the reasons set forth above, the judgment of the district court must be reversed.

Respectfully submitted,

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DATED: Lynchburg, Virginia
November 13, 1975

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8. The usual rule is that a jury demand must be made in the first responsive pleading filed in court. However, in this case, judgment was entered before a responsive pleading could be filed and therefore defendant is entitled to demand a trial by jury.

Sec V Allan - .

STATE OF NEW YORK)
: SS.
COUNTY OF NEW YORK)

ROBERT BAILEY, being duly sworn, deposes and says, that deponent is not a party to the action, is over 18 years of age and resides at 286 Richmond Avenue, Staten Island, N.Y. 10302. That on the 18 day of Nov
1975 deponent served the within Brief upon: Securities + Exchange Comm.
Sec.

attorney(s) for Appellee

in this action, at 26 Federal Plaza - Dept of Justice
N Y C. Washington, D.C.

the address(es) designated by said attorney(s) for that purpose by depositing 3 true copies of same enclosed in a postpaid properly addressed wrapper, in an official depository under the exclusive care and custody of the United States post office department within the State of New York.

Robert Bailey

Sworn to before me, this 18
day of Nov, 1975.

William Bailey

WILLIAM BAILEY
Notary Public, State of New York
No. 43-0132945
Qualified in Richmond County
Commission Expires March 30, 1976